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# **The G20/OECD Principles of Corporate Governance 2015: A Critical Assessment of its Operation and Impact**

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*Abstract: The OECD promotes the 2015 version of the Principles of Corporate Governance as a means ‘to support investment as a powerful driver of growth’. But how realistic is this ambition? This paper provides a critical assessment of the operation and impact of these Principles. It maps the governance model of the Principles and discusses their impact on state legislation and at the firm level. It concludes there are various problems with the operation of the Principles as far as they are regarded as a universal benchmark, while they can be a useful ‘common frame of reference’ for the debate about corporate governance reform in academia and practice.*

## **1. Introduction**

The Organisation for Economic Co-operation and Development (OECD) promotes the G20/OECD Principles of Corporate Governance 2015 as a means ‘to support investment as a powerful driver of growth’.<sup>1</sup> Indeed, there may be reasons why the OECD could be confident about the impact of its Principles of Corporate Governance. The 34 members and five partner countries of the OECD belong to the wealthiest of the world and account for 80% of world trade and investment.<sup>2</sup> Beyond its members and partners, the OECD plays an important role at a global scale since its recommendations are often aimed at the law makers of less developed countries and businesses themselves. For example, its Principles of Corporate Governance (in the following: ‘Principles’) are intended to assist governments as well as stock exchanges, investors and private corporations in the improvement of their corporate governance institutions.<sup>3</sup>

The question remains, however, how realistic this ambition of the OECD is and how satisfactory the Principles operate across the world. Since the adoption of the first version of the Principles in 1999 researchers have examined whether and how they have been applied in countries of Africa and the Middle East,<sup>4</sup> Europe and Asia,<sup>5</sup> and Latin

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\* Durham University and Kent University. A previous version of this paper, dealing with the 2004 version of the principles, was published under the title ‘The OECD Principles of Corporate Governance in Emerging Markets: A successful example of networked governance?’, in M Fenwick, S Van Uytsel and S Wrška (eds), *Networked Governance, Transnational Business and the Law* 257-284 (Berlin: Springer 2014). Relevant parts are reprinted with permission. We thank conference and seminar participants at Kyushu University (Fukuoka, Japan), Tsinghua University (Beijing, China) and the Institute of Advanced Legal Studies (London, UK) for helpful comments.

<sup>1</sup> G20/OECD Principles of Corporate Governance 2015 at p 3.

<sup>2</sup> History of the OECD, available at [www.oecd.org/about/history/](http://www.oecd.org/about/history/).

<sup>3</sup> For references and details see 2., below.

<sup>4</sup> DA Guobadia, ‘The Rules of Good Corporate Governance and the Methods of Efficient Implementation: A Nigerian Perspective’ (2001) 22 *Company Lawyer* 119; AM Abu-Tapanjeh, ‘Corporate Governance from the Islamic Perspective: A Comparative Analysis with OECD Principles’ (2009) 20 *Critical Perspectives on Accounting* 556; Z Sharar ‘The Board of Directors of Public Companies: A Comparative

America.<sup>6</sup> The present paper is, however, the first one that addresses the 2015 version of the Principles. It also different from previous research in discussing the Principles at a general conceptual level, while also considering the operation at the ground level.

The corresponding structure of this paper is as follows. Section 2 sets the scene in providing an introduction into the evolution and core elements of the Principles. Section 3 addresses the impact of the Principles, both in terms of state legislation and the ‘micro-level’, taking Mexico as an example. The critical assessment in section 4 examines the substantive fit of the Principles. It also uses the concepts of ‘networked governance’ and ‘wicked problems’ in order to evaluate the nature and operation of the Principles. Section 5 concludes.

## 2. Evolution and core elements of the Principles

The initial version of the Principles was adopted in 1999 and the revised one in 2004.<sup>7</sup> Both versions were drafted in the aftermath of financial crises, namely, the Asian financial crisis and the ‘dot-com bubble’. This was also reflected in their aims, for example, the Foreword to the Principles 2004 referring to the contribution good corporate governance to financial market stability.

Following the global financial crisis of 2008, initially, the OECD saw ‘no immediate call for a revision of the OECD Principles’.<sup>8</sup> But, in 2013, in line with other discussions about corporate governance reform after the crisis,<sup>9</sup> the OECD also initiated a revision

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Analysis of the Corporate Governance Framework in the State of Qatar and Australia, Measured Against the OECD Principles of Corporate Governance’ (2010) 1 *The Legal & Judicial Journal-Ministry of Justice-State of Qatar* 201, available at <http://ssrn.com/abstract=1701063>; MA Al-Saeed, ‘Compliance with the Principles of Corporate Governance: Different Perspectives from Jordan’ (2012) 22 *Global Journal of Management and Business Research* 13.

<sup>5</sup> L Tspouri and M Xanthakis, ‘Can Corporate Governance be Rated? Ideas based on the Greek experience’ (2004) 12 *Corporate Governance: An International Review* 16; F Jesover, ‘Corporate Governance in the Russian Federation: The Relevance of the OECD Principles on Shareholder Rights and Equitable Treatment’ (2001) 9 *Corporate Governance: An International Review* 79; J Iu and J Batten J, ‘The Implementation of OECD Corporate Governance Principles in Post-Crisis Asia’ (2001) 4 *The Journal of Corporate Citizenship* 47; VZ Chen, J Li and DM Shapiro, ‘Are OECD-prescribed ‘Good Corporate Governance Practices’ Really Good in an Emerging Economy?’ (2011) 28 *Asia Pacific Journal of Management* 115; IA Khan, ‘The Role of International Organisations in Promoting Corporate Governance in Developing Countries: A Case Study of Pakistan’ (2012) 23 *International Company and Commercial Law Review* 223.

<sup>6</sup> CH Kitagawa and MS Ribeiro, ‘Governança corporativa na América Latina: a relevância dos princípios da OCDE na integridade dos conselhos e autonomia dos conselheiros’ (2009) 20 *Revista Contabilidade & Finanças* 61; O Alvarez-Macotela, *Securities Law and Informal Redress: An Institutional Analysis of Equity Market Development in Mexico (1975-2005)*, PhD thesis, University of East Anglia, Norwich, 2008, p 125.

<sup>7</sup> See generally [www.oecd.org/daf/ca/oecdprinciplesofcorporategovernance.htm](http://www.oecd.org/daf/ca/oecdprinciplesofcorporategovernance.htm). In addition, the OECD has published Guidelines on Corporate Governance of State Owned Enterprises and Guidelines on Multi-national Enterprises, not discussed in this paper.

<sup>8</sup> OECD, ‘Corporate Governance and the Financial Crisis: Key Findings and Main Messages’ (2009) available at [www.oecd.org/daf/ca/corporategovernanceprinciples/43056196.pdf](http://www.oecd.org/daf/ca/corporategovernanceprinciples/43056196.pdf). See also [www.oecd.org/daf/ca/corporategovernanceprinciples/corporategovernanceandthefinancialcrisis.htm](http://www.oecd.org/daf/ca/corporategovernanceprinciples/corporategovernanceandthefinancialcrisis.htm).

<sup>9</sup> For the discussion see, eg, J Mukwiri and M Siems, ‘The Financial Crisis: A Reason to Improve Shareholder Protection in the EU’ (2014) 41 *Journal of Law and Society* 51; D Arsalidou and M Krambia-

of the Principles. Following the parallel development of a closer cooperation between the OECD and the G20,<sup>10</sup> the leaders of the G20 endorsed the revised OECD Principles in November 2015, which therefore became the G20/OECD Principles of Corporate Governance 2015.<sup>11</sup>

A difficult question is what forces have shaped the Principles and therefore what interests they may favour. The restricted membership of the OECD means that is sometimes seen as a ‘rich man’s club’.<sup>12</sup> However, there has also been some variation in its approach. When the OECD was founded in 1961, it followed a centre-left Keynesian line but in the 1980s it became more ‘neoliberal’, notably with a study on Structural Adjustment and Economic Performance in 1987 and with the unsuccessful negotiations for a Multilateral Agreement on Investment in the mid 1990s. Today, a mixed policy is said to be dominant, not least due to the strong position of European countries.<sup>13</sup> Sometimes it is also said that the OECD is shaped by its ‘expert culture’,<sup>14</sup> thus with its staff acting with a degree of independence from the member countries.

The drafting of the 1999 and 2004 version of the Principles has been praised as an example of an inclusive process that protects and promotes a wider common interest.<sup>15</sup> It involved a variety of other actors: the OECD’s Business and Industry Advisory Committee (BIAC) and Trade Union Advisory Committee (TUAC) contributed to the drafting process, the World Bank and the International Monetary Fund (IMF) participated as observers, regional roundtables and further meetings consulted with non-member countries, and a public consultation was conducted.<sup>16</sup> A similar picture emerges from the process of the 2013-2015 revision: as the OECD explains, the review ‘benefited from consultations with stakeholders, including the business sector, investors, professional groups at national and international levels, trade unions, civil society organisations and other international standard setting bodies.’<sup>17</sup>

Despite this inclusive procedure, it has been suggested that the Principles were mainly shaped by the lobbying of international institutional investors, in particular through the International Corporate Governance Network (ICGN), representing institutional investors who represent funds of more than 18 trillion US Dollars.<sup>18</sup> This influ-

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Kapardis, ‘Weak Corporate Governance can Lead to a Country’s Financial Catastrophe: The Case of Cyprus’ (2015) *Journal of Business Law* 361.

<sup>10</sup> See [www.oecd.org/g20/about.htm](http://www.oecd.org/g20/about.htm) (it started with the G20-Pittsburgh Summit in 2009).

<sup>11</sup> See [www.oecd.org/daf/ca/g20-leaders-endorse-g20-oecd-principles-of-corporate-governance.htm](http://www.oecd.org/daf/ca/g20-leaders-endorse-g20-oecd-principles-of-corporate-governance.htm)

<sup>12</sup> See 3.1, below.

<sup>13</sup> See R Mahon and S McBride, ‘Introduction’, in *The OECD and Transnational Governance* (R Mahon and S McBride eds, Vancouver: UBC Press 2008) 3 at 14; R McBride and S Mahon, ‘Conclusion’, in *ibid* 276 at 279. For the ongoing attempts of the OECD to liberalise investment see RA Williams, ‘The OECD and Foreign Investment Rules: The Global Promotion of Liberalization’, in *ibid* 117.

<sup>14</sup> K Martens and AP Jakobi, ‘Introduction’, in *Mechanisms of OECD Governance: International Incentives for National Policy-Making?* (K Martens and AP Jakobi eds, Oxford: OUP 2010) 1 at 14.

<sup>15</sup> A Baker ‘The “Public Interest” Agency of International Organizations? The Case of the OECD Principles of Corporate Governance’ (2012) 19 *Review of International Political Economy* 389.

<sup>16</sup> See L Bouchez, ‘Principles of Corporate Governance: the OECD Perspective’ (2007) 4 *European Company Law* 109 at 109-110; S Fazio, ‘Corporate Governance, Accountability and Emerging Economies’ (2008) 29 *Company Lawyer* 105 at 107.

<sup>17</sup> See [www.oecd.org/corporate/2014-review-oecd-corporate-governance-principles.htm](http://www.oecd.org/corporate/2014-review-oecd-corporate-governance-principles.htm).

<sup>18</sup> T Porter and M Webb, ‘Role of the OECD in the Orchestration of Global Knowledge Networks’ in *The OECD and Transnational Governance* (R Mahon and S McBride eds, Vancouver: UBC Press 2008) 43.

ence could derive from the expectation that legal unification can reduce the costs of investing in companies from more than one country.<sup>19</sup> It is also akin to the view that the Principles are a one-sided promotion of Anglo-Saxon corporate governance with an emphasis on shareholder primacy.<sup>20</sup>

However, the substance of the Principles does not support such a position. In the Preamble, they explain that ‘there is no single model of good corporate governance’, but that they aim to build on their ‘common elements’.<sup>21</sup> This search for commonalities is also reflected in the Principles’ coverage of the mainstream topics of corporate governance, such as the rights of shareholders and the responsibilities of the board.<sup>22</sup> In other instances, choices have been made: for example, the statement that there should be a ‘sufficient number of non-executive board members capable of exercising independent judgement’<sup>23</sup> is based on the use of independent board members in Anglo-Saxon countries. By contrast, the sections on the role of stakeholders in corporate governance<sup>24</sup> are apparently based on continental European models.<sup>25</sup>

The 2015 version of the Principles kept the main substance and structure unchanged. It added, however, a section on ‘institutional investors, stock markets, and other intermediaries’ with the aim to ensure the integrity of conduct in the investment chain.<sup>26</sup> These provisions reflect recent problems, in particular for cross-border situations, as well as the general trend that questions of company and securities are increasingly seen as interrelated. Similarly, the other new provisions are about new topics that have been discussed and/or implemented in many countries, for example, shareholder participation in decisions on executive remuneration, the risk oversight responsibilities of boards, the use of specialised board committees and the importance of board diversity.<sup>27</sup>

Beyond those specific rules, it is noticeable that the Principles have been formulated in a general fashion. This is deliberate, as they are not supposed to be a uniform ‘Act’ but to offer different possibilities as to how good corporate governance practices can be achieved. This can also be seen in the way the Principles are meant to operate.

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The ICGN has also developed its own Global Corporate Governance Principles, see <https://www.icgn.org/policy>.

<sup>19</sup> The aspiration to reduce transaction costs is a frequent topic in the literature on harmonisation: see, eg, U Mattei, *Comparative Law and Economics* (Ann Arbor: University of Michigan Press 1997) 94, 219.

<sup>20</sup> S Soederberg, ‘The Promotion of ‘Anglo-American’ Corporate Governance in the South: Who Benefits from the New International Standard?’ (2003) 24 *Third World Quarterly* 7.

<sup>21</sup> G20/OECD Principles of Corporate Governance 2015, p 10.

<sup>22</sup> G20/OECD Principles of Corporate Governance 2015, s II and VI.

<sup>23</sup> G20/OECD Principles of Corporate Governance 2015, s VI.E1.

<sup>24</sup> G20/OECD Principles of Corporate Governance 2015, s IV and VI.C.

<sup>25</sup> See also Baker, *supra* note 15, at 397 (on compromise nature of Principles); A Kaufman and E Englander, ‘A Team Production Proposal to the Shareholder - Stakeholder Quarrel: The OECD Principles of Corporate Governance’ (2006), available at <http://ssrn.com/abstract=1030846>; L Ceroni, ‘Corporate Governance: the OECD Principles, the Scope for a “Model of the Successful Company”, and a New Challenge for the Company Law Agenda and the Broader Regulatory Agenda’ (2008) 5 *Corporate Ownership and Control* 268.

<sup>26</sup> G20/OECD Principles of Corporate Governance 2015, s III.

<sup>27</sup> G20/OECD Principles of Corporate Governance 2015, s II.C.4, VI.D.1, E.2 and 4.

**Fig. 1: Overview of the functioning of the Principles**

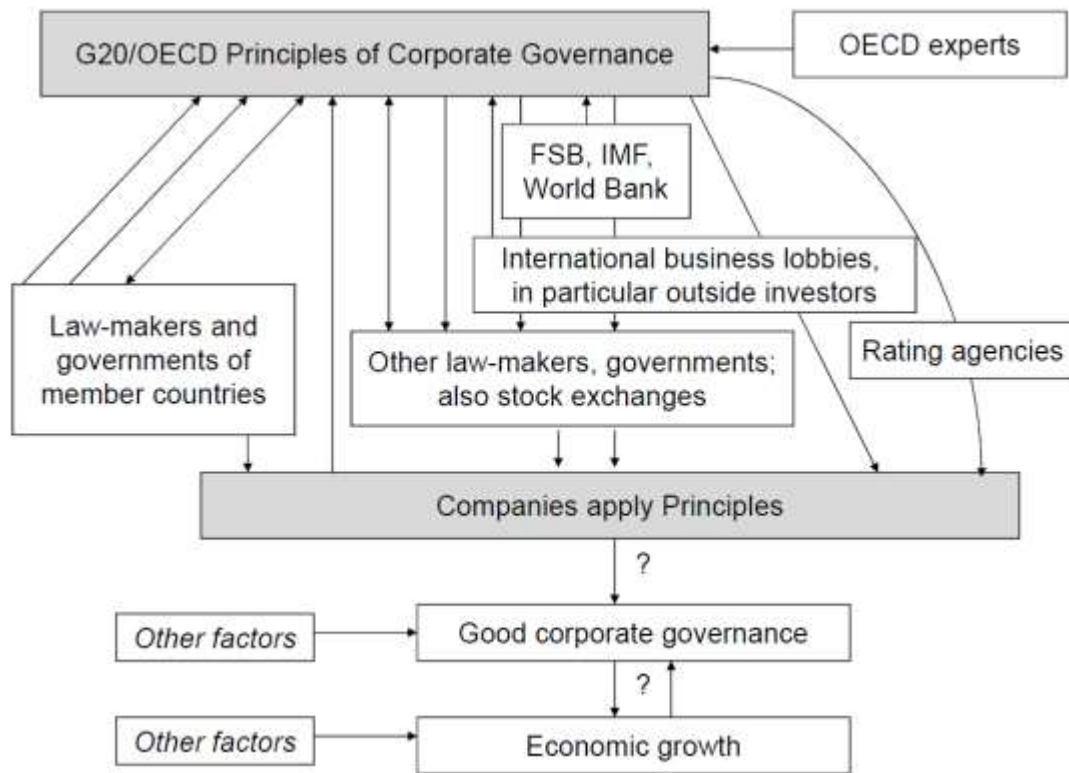


Figure 1 illustrates this complexity of the impact of the Principles (as well as their drafting, as already discussed). In the first instance, the Principles are soft law aimed at law makers in less developed economies, which includes stock-exchanges as far as they decide on corporate governance rules for listed companies.<sup>28</sup> However, the voluntariness of the Principles can be reduced in practice: the Financial Stability Board (FSB), the World Bank and the IMF regard the Principles as one of the international standards countries are urged to adopt.<sup>29</sup> The implementation of the Principles can also be the result of market pressure, namely as far as countries want to stimulate foreign investment.<sup>30</sup>

At the level of companies, they may simply have to apply domestic laws based on the Principles. In addition, as far as those laws leave options for companies, the Principles function as guidance for good practice, in particular for larger companies.<sup>31</sup> Here too, then, it may matter that companies would be interested in implementing the Principles in order to attract investments, for example, by way of improving investor

<sup>28</sup> See generally H Christiansen and A Koldertsova, 'The Role of Stock Exchanges in Corporate Governance' (2009) 1 *Financial Market Trends* 1.

<sup>29</sup> See 3.1, below.

<sup>30</sup> Though it is doubtful whether such a positive relationship between adopting international benchmarks and foreign investment actually exists. See A Perry-Kessaris, 'Finding and Facing Facts about Legal Systems and Foreign Direct Investment in South Asia' (2003) 23 *Legal Studies* 649.

<sup>31</sup> G20/OECD Principles of Corporate Governance 2015, p 4 (indicating that 'some of the Principles may be more appropriate for larger than for smaller companies').

protection or by way reducing the costs of legal diversity.<sup>32</sup> This is also fostered by the fact that some rating agencies use the Principles in order to rank the quality of firm-level corporate governance.<sup>33</sup>

Both these elements, the country and the firm level, will be discussed in further detail in the next section, using Mexico and, to a lesser extent, Brazil and Russia as examples.

### 3. The Impact of the Principles

#### 3.1 Impact on state legislation

The laws of most developed countries widely correspond to the Principles.<sup>34</sup> Moreover, as far as law makers have not incorporated all elements of the Principles, corporate governance codes operating on a ‘comply or explain’ basis may step in. Here, the expectation is that institutional investors have sufficient expertise to monitor the right level of compliance with good corporate governance practices. By contrast, in other parts of the world – notably in countries that have (or used to have) autocratic political regimes – there may be insufficient experience with a distinction between rules that ‘must’ and ‘may’ be adopted. Thus, here, it seems to be more likely that law makers simply impose good corporate governance standards by way of binding rules.<sup>35</sup>

Another point to consider is whether a country is a member of the OECD. For example, this may lead to a different situation for Mexico and Brazil since only Mexico is a member of the OECD, having joined in 1994.<sup>36</sup> There have also been discussions about a possible membership of Brazil. In 2010, the OECD Deputy Secretary General Richard Boucher indicated that the OECD would ‘love to have Brazil as a member’.<sup>37</sup> However, he also expressed the view that this may be contentious as the OECD ‘has historically been seen as somewhat of a “rich man’s club”’. Indeed a Brazilian politician even took the position that joining the OECD would be ‘political suicide’, claiming that Mexico became isolated in Latin America due to its membership of the OECD and NAFTA in the early 1990s.<sup>38</sup>

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<sup>32</sup> See also Center for International Private Enterprise, ‘Impact on Reform: Corporate Governance Flyer’ 2011, available at [www.cipe.org/sites/default/files/publication-docs/corporateGovernance.pdf](http://www.cipe.org/sites/default/files/publication-docs/corporateGovernance.pdf) (‘in emerging markets all over the world, corporate governance can give companies a competitive edge’).

<sup>33</sup> See H Sherman, ‘Corporate Governance Ratings’ (2004) 12 *Corporate Governance: An International Review* 5.

<sup>34</sup> References in M Siems, *Convergence in Shareholder Law* (Cambridge University Press, Cambridge, 2008) at 227.

<sup>35</sup> See also the discussion of the situation in Mexico in 3.2, below.

<sup>36</sup> P Carroll and A Kellow, *The OECD: A Study of Organisational Adaptation* (Cheltenham: Elgar 2011) at 259 (noting that Mexican membership aimed to ensure regional balance as some Eastern European countries also joined). For the list of OECD members see [www.oecd.org/general/listofocdmemberscountries-ratificationoftheconventionontheoecd.htm](http://www.oecd.org/general/listofocdmemberscountries-ratificationoftheconventionontheoecd.htm).

<sup>37</sup> Brazil already participates in some of the OECD bodies. See M Schewel, ‘OECD Deputy Secretary General Eyes Brazil as a Potential Member’ *The Inter-American Dialogue* 2010, available at <http://archive.thedialogue.org/page.cfm?pageID=32&pubID=2306>; M Ougaard, ‘The OECD’s Global Role: Agenda-setting and Policy Diffusion’ in *Mechanisms of OECD Governance: International Incentives for National Policy-making?* (K Martens and AP Jakobi eds, Oxford: OUP 2010) 26 at 41-42.

<sup>38</sup> PRLog.Org ‘Brazil would commit political suicide by joining the OECD, says ex-finance minister Rubens Ricupero’ Press release 11 June 2009, available at <https://www.prlog.org/10256031-brazil-would->

One of the requirements for joining the OECD is a country's 'positioning' to the existing OECD instruments,<sup>39</sup> also described as 'voluntary but constrained policy transfer'.<sup>40</sup> The roadmap for Russia's accession illustrates that a review of corporate governance policies such as the Principles can play an important role.<sup>41</sup> Mexico already joined the OECD before the first version of the Principles was enacted in 1999. Thus, for Mexico a first point to note is that the Principles are categorised as 'recommendations', as distinguished from 'decisions' of the OECD, meaning that they are not legally binding on the member countries.<sup>42</sup> Moreover, the OECD has no formal enforcement powers but assesses the policies of its member countries by way of peer reviews and surveys. While some of these peer reviews evaluate the policies of a particular country in detail, the Principles are not included in these country studies.<sup>43</sup> However, in 2011 the OECD started a limited thematic peer review on the application of the Principles: the six reports contain interesting comparative information on selected countries and topics,<sup>44</sup> while they do not provide a clear policy assessment about the general compliance of particular countries with the Principles as a whole.

In addition, we need to consider the influence of the FSB, the IMF and the World Bank. Both Mexico and Brazil are members of the FSB. The Principles are part of the so-called Compendium of Standards which the members have 'accepted as important for sound, stable and well functioning financial systems'.<sup>45</sup> Yet, the FSB does not evaluate the implementation of the standards itself, but considers the reviews of the IMF and the World Bank, namely the reports of the Financial Sector Assessment Program (FSAP) and the Reports on the Observance of Standards and Codes (ROSCs).<sup>46</sup> In the FSAP reports some references to sound corporate governance are made, yet, without going into details of the Principles.<sup>47</sup> By contrast, the ROSCs of the World Bank examine each individual aspect of the Principles in order to assess a country's quality of corporate governance, based on a methodology developed by the OECD.<sup>48</sup> This interest of

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commit-political-suicide-by-joining-the-oecd-says-exfinance-minister-rubens-ricupero.html (quoting the former Brazilian Finance Minister Rubens Ricupero).

<sup>39</sup> See <http://www.oecd.org/about/membersandpartners/enlargement.htm>.

<sup>40</sup> Carroll and Kellow, *supra* note 36, at 164.

<sup>41</sup> See [www.oecd.org/russia/therussianfederationandtheoecd.htm](http://www.oecd.org/russia/therussianfederationandtheoecd.htm) and [www.oecd.org/daf/corporateaffairs/russia](http://www.oecd.org/daf/corporateaffairs/russia).

<sup>42</sup> See <http://webnet.oecd.org/oecdacts/> (search for 'recommendations') and [www.oecd.org/legal/legal-instruments.htm](http://www.oecd.org/legal/legal-instruments.htm).

<sup>43</sup> See [www.oecd.org/site/peerreview/](http://www.oecd.org/site/peerreview/) and, eg, Martens and Jakobi, *supra* note 14, at 10-11; Porter and Webb, *supra* note 18, at 49-52.

<sup>44</sup> Reports on 'Board Practices: Incentives and Governing Risks, Corporate Governance' (2011), 'The Role of Institutional Investors in Promoting Good Corporate Governance' (2011), 'Related Party Transactions and Minority Shareholder Rights' (2012), 'Board Member Nomination and Election' (2012), 'Supervision and Enforcement in Corporate Governance' (2013), 'Risk Management and Corporate Governance' (2014) all available at <http://www.oecd.org/corporate/principles-corporate-governance.htm>. A similar selective report is International Organization of Securities Commissions (IOSCO), 'Board Independence of Listed Companies: Final Report from the Technical Committee of the IOSCO in consultation with the OECD' (2007), available at [www.iosco.org/library/pubdocs/pdf/IOSCOPD238.pdf](http://www.iosco.org/library/pubdocs/pdf/IOSCOPD238.pdf).

<sup>45</sup> See [www.financialstabilityboard.org/cos/index.htm](http://www.financialstabilityboard.org/cos/index.htm).

<sup>46</sup> See [www.financialstabilityboard.org/activities/peer\\_reviews.htm](http://www.financialstabilityboard.org/activities/peer_reviews.htm).

<sup>47</sup> See [www.imf.org/external/np/fsap/fssa.aspx](http://www.imf.org/external/np/fsap/fssa.aspx).

<sup>48</sup> See [www.worldbank.org/ifa/rosc\\_cg.html](http://www.worldbank.org/ifa/rosc_cg.html); also [www.imf.org/external/NP/rosc/rosc.aspx](http://www.imf.org/external/NP/rosc/rosc.aspx). In 2007, the European Bank for Reconstruction and Development (EBRD) conducted a similar assessment for the countries of Eastern Europe and Central Asia: European Bank for Reconstruction and Development



the World Bank in corporate governance is also reflected in the Global Corporate Governance Forum (GCGF), in 1999 co-founded together with the OECD, and now part of the World Bank with the OECD as a ‘donor partner’.<sup>49</sup>

However, the effect of the ROSCs should also not be overstated. The ROSCs are not conducted on a regular basis but only when a country asks for such an assessment, in particular, when it requires significant loans from the IMF and the World Bank.<sup>50</sup> In 2007, the OECD also published a document explaining how the ROSCs should assess the implementation of the Principles. Implementation is assessed in relative terms, namely as fully, broadly, partly or not implemented. Moreover, the OECD takes the view that ‘outcomes’ matter, meaning that functional equivalents are also accepted.<sup>51</sup> But, here then, it also needs to be considered that in practice countries may well feel that they should comply with the Principles in exactly the way they are phrased in the text: there is no catalogue of what ‘functional equivalents’ may be acceptable, and the ‘box-ticking nature’ of the ROSCs provides an incentive to fully comply with them – and not to come up with a different solution.

In the case of Mexico and Brazil, the most recent ROSCs of the Principles are from 2003 and 2005, respectively.<sup>52</sup> By contrast to more recent ROSCs of other countries, the assessments do not provide aggregate scores for compliance with the Principles and their main sub-categories. However, it can be seen that the results are somehow mixed with the most frequent categories ‘broadly’ or ‘partly’ implemented. This does not necessarily mean that the Principles had no effect in these countries. In Mexico and Brazil corporate governance has become a major topic since the late 1990s. In particular, in both countries voluntary codes of good corporate governance have been issued and subsequently updated. This process has been identified because of the Principles.<sup>53</sup> Unlike Mexico,<sup>54</sup> in Brazil a further voluntary improvement of corporate governance has been implemented by way of a premium segment of the stock market with a higher level of shareholder protection (the Novo Mercado).<sup>55</sup> In a quantitative study by one of us, it has also been shown that the level of shareholder protection increased in both Mexico and Brazil between 1990 and 2013.<sup>56</sup>

It is interesting to note that the World Bank’s more recent ROSCs of the Principles also refer to another set of indicators, namely the performance of countries in the ‘protecting investors’ indicators of the World Bank’s Doing Business Report.<sup>57</sup> The desire

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(EBRD), see [www.ebrd.com/what-we-do/sectors/legal-reform/corporate-governance/sector-assessment.html](http://www.ebrd.com/what-we-do/sectors/legal-reform/corporate-governance/sector-assessment.html).

<sup>49</sup> See [www.gcgf.org](http://www.gcgf.org).

<sup>50</sup> See Khan, *supra* note 5, at 225.

<sup>51</sup> See OECD, ‘Methodology for Assessing the Implementation of the OECD Principles of Corporate Governance’ (2007), available [www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/37776417.pdf](http://www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/37776417.pdf) at pp 9-14.

<sup>52</sup> They are available at [www.worldbank.org/ifa/rosc\\_cg.html](http://www.worldbank.org/ifa/rosc_cg.html).

<sup>53</sup> For Mexico see Alvarez-Macotella, *supra* note 6. For Brazil see Fazio, *supra* note 16, at 111.

<sup>54</sup> See 3.2, below.

<sup>55</sup> See RJ Gilson, H Hansmann and M Pargendler, ‘Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union’ (2011) 63 *Stanford Law Review* 475.

<sup>56</sup> See D Katelouzou and M Siems, ‘Disappearing Paradigms in Shareholder Protection: Leximetric Evidence for 30 Countries, 1990-2013’ (2015) 15 *Journal of Corporate Law Studies* 127.

<sup>57</sup> See, eg, World Bank, Report on the Observance of Standards and Codes (ROSC): Corporate Governance Country Assessment - The Kingdom of Morocco, June 2010, available at [www.worldbank.org/ifa/rosg\\_cg\\_morocco\\_2010\\_eng.pdf](http://www.worldbank.org/ifa/rosg_cg_morocco_2010_eng.pdf), at p 33.

to reduce the differences between both sets of indicators can also be seen in the 2015 revision of the Principles as it inserted detailed provisions on ‘related party-transactions’ of directors and executives,<sup>58</sup> apparently influenced by the treatment of this topic in the Doing Business Report.<sup>59</sup>

Another, more contextual, recent approach is that the OECD starts with the Principles but then uses regional roundtables in order to address some of the more specific local problems. For example, a Roundtable for Latin America has met on annual basis dealing with a variety of topics since the year 2000.<sup>60</sup>

This latter trend has also led to two empirical investigations of the situation in Latin American countries. A paper by Carlos Henrique Kitagawa and Maísa de Souza Ribeiro compared the board integrity and director independence in Argentina, Brazil, Chile and Mexico.<sup>61</sup> This was based on nine questions on problems outlined in the OECD White Paper on Corporate Governance in Latin America from 2003.<sup>62</sup> With respect to the positive law, the result is somehow mixed, for instance, most of the countries have only few, if any, legislation on board committees; overall, however, Mexico is said to have a higher rate of compliance than the other three countries.

Another study was conducted by the OECD itself, dealing with the same countries plus Columbia, Panama and Peru.<sup>63</sup> This study uses the Principles from 2004 as a starting point but also refers to the aforementioned White Paper. Here again, the result is somehow mixed but relatively similar in most of the countries: compliance in the main categories but not with regard to some of the more specific recommendations, such as the responsibility of boards to engage in risk management and internal evaluations.

As both of these studies were based on firm surveys, they also address how far companies actually complied with those recommendations. The need for such a law-in-practice perspective is in line with the more general position of the OECD. It is said that:

[T]he Principles should be considered a living document. It is an OECD priority to make sure that they are widely disseminated and actively used. This will include a continuing policy dialogue where policymakers, regulators and standard-setters will be able to exchange practical experience of implementing the Principles.<sup>64</sup>

A recent journal article by Andrew Baker has praised the Principles for such ‘experimental deliberative governance’.<sup>65</sup> It also appears plausible that in Latin America an

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<sup>58</sup> G20/OECD Principles of Corporate Governance 2015, s II.F.

<sup>59</sup> See <http://www.doingbusiness.org/methodology/protecting-minority-investors>.

<sup>60</sup> See [www.oecd.org/daf/ca/latinamericanroundtableoncorporategovernance.htm](http://www.oecd.org/daf/ca/latinamericanroundtableoncorporategovernance.htm).

<sup>61</sup> Kitagawa and Ribeiro, *supra* note 6.

<sup>62</sup> OECD, ‘White Paper on Corporate Governance in Latin America’ (2003), available at [www.oecd.org/dataoecd/25/2/18976210.pdf](http://www.oecd.org/dataoecd/25/2/18976210.pdf).

<sup>63</sup> OECD, ‘Achieving Effective Boards: A comparative study of corporate governance frameworks and board practices in Argentina, Brazil, Chile, Colombia, Mexico, Panama and Peru’ (2011), available at [www.oecd.org/countries/panama/48510039.pdf](http://www.oecd.org/countries/panama/48510039.pdf).

<sup>64</sup> F Jesover and G Kirkpatrick, ‘The Revised OECD Principles of Corporate Governance and their Relevance to Non-OECD Countries’ (2005) 13 *Corporate Governance: An International Review* 127 at 128-129 (note that both authors work for the OECD). The role of enforcement has also been stressed following the financial crisis of 2008, see 2. above.

<sup>65</sup> Baker, *supra* note 15.

OECD-sponsored initiative called ‘Companies Circle’ has the aim to share best practice between companies and provide feedback to the Latin American Roundtable.<sup>66</sup> Yet, the following will also present a more nuanced perspective of the ‘Principles in context’, using Mexico as an example.

### *3.2 The operation of the Principles at the ‘micro-level’*

In Mexico, the implementation of the Principles has partly been driven by the federal government. But the coordination efforts have also been both based *on* and influenced *by* networks of stakeholders. Importantly for the purpose of our analysis, those networks have consisted of peers (eg, gremial organisations and associations of companies by economic sector and by federations of businesses organisations), but also of stakeholders across sectors, geographical regions within Mexico and internationally. Yet, overall, most influential has been a proactive attitude towards the Principles by Mexico’s government and by the leading financial and businesses associations.

Mexico’s proactive approach on the topic obeys to the strategic importance that its membership to the OECD has represented for the Mexican government and to the promising scenario it creates for Mexico’s private sector,<sup>67</sup> more specifically among the elite businesses that are capable and willing to compete in the global markets. Private sector efforts have been orchestrated by the Business Co-ordinator Council (CCE by its initials in Spanish). Mexico has also shown some leadership in matters of corporate governance: Mexico’s code of best corporate practices adopting the Principles (hereafter ‘the Code’) was the first in Latin America and one of the first in the world. The CCE has produced a number of guidelines, testimonials, practical examples in order to facilitate implementation of the Code and related material,<sup>68</sup> being the result of intensive and co-ordinated interplay between several domestic nodes of further networks in Mexico and across countries.

The main audit firms (Deloitte, KPMG, Ernst & Young, PwC, etc.) were actively involved. Deloitte, in particular has played a leading role in the every-day implementation of the Principles in Mexico by means of its partnership with the World Bank and the Centre of Excellence in Corporate Governance (CEGC by its initials in Spanish).<sup>69</sup> The CEGC has also developed an original Corporate Governance Index that helps companies in their self-assessment relative to the codes of best practices.<sup>70</sup> Moreover, the CEGC publishes scores on the average compliance of Mexican firms with the Principles, thus supplementing the ROSCs which just look at the quality of implementation based on the positive law.

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<sup>66</sup> See [www.oecd.org/brazil/corporategovernanceinlatinamerica.htm](http://www.oecd.org/brazil/corporategovernanceinlatinamerica.htm).

<sup>67</sup> According to A Chong and F Lopez-de-Silanes, ‘Corporate Governance and Firm Value in Mexico’ in *Investor Protection and Corporate Governance: Firm-level Evidence Across Latin America* (A Chong and F Lopez-de-Silanes eds, Palo Alto: Stanford University Press 2007) 397 at 433: ‘Mexico was concerned about corporate governance mainly as a result of the lack of growth in domestic markets and the damaging experience in East Asia, where economies were emerging from the 1997-98 crisis...’.

<sup>68</sup> Available at [www.cce.org.mx/CMPC/](http://www.cce.org.mx/CMPC/).

<sup>69</sup> See CEGC ‘Historia’ available at <http://web.uas.mx/cegc/x2000-cegc.asp?titulosec=10> and ‘Programa de Desarrollo para Consejeros’ (Development Program for Directors), available at <http://ols.uas.mx/cegc/programa/default.asp>.

<sup>70</sup> See <http://web.uas.mx/cegc/x2000-cegc.asp?titulosec=27>.

This variety of institutional actors is essential to the operation of the Principles in Mexico. However, this can also lead to complex challenges. This is not so much due to the number and variety of them but in view of the combination of formal and informal networks among those groups. For example, consider the Mexican stock market: the key players in this market are the financial intermediaries, listed companies and investors, plus the financial authority. Each of these groups has created formal networks among them.<sup>71</sup> However, it cannot be assumed that those groups are defined and constrained by conventional borders. There is an informal overlapping of roles that conventional wisdom assumes to the role played by different economic agents, in this case investors, listed firms and financial intermediaries.<sup>72</sup> The roles of investors and intermediaries are also blurred because of strategic alliances. Previous securities law and its enforcement were insufficient to upgrade the levels of trust by investors in local stock-brokers, which partly explains an informal solution where foreign investors started participating in the Mexican equity market by bringing with them their trusted financial intermediaries.<sup>73</sup>

Potentially problematic is the strategy of the Mexican law maker. In 2005, it enacted a new securities market law (SML) and substantially revised the existing company law. The new SML created three new types of public companies, namely the SAPI, the SAPIB, and the SAB,<sup>74</sup> whereby all firms listed on the MSE must be SABs. This new approach to securities law means that the SML ended up regulating not only listed firms but also some non-listed companies.<sup>75</sup> It makes mandatory to comply with the Code but at different degrees, depending on the type of corporation. As articulated by Sam Podolsky in an OECD publication:

The new law enforces Corporate Governance for SAPIs even though they are not publicly traded! And (...) makes a legal obligation for publicly held corporations to comply with modern practices of corporate governance (it is not voluntary an-

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<sup>71</sup> Brokerage firms via the AMIB and the Mexican Stock Exchange (MSE); banks via the AMB; listed firms via the CCE and the Mexican Association of Investor Relations (AMERI); investors via the Mexican Association of Independent Investment Advisers (AMAI) and, indirectly, via collective investments such as pension and mutual funds, and the financial authority via organisations such as the IOSCO.

<sup>72</sup> Some of the wealthiest families are simultaneously investors, controlling shareholders of listed firms and financial intermediaries. Financial firms also invest in the market, and non-financial firms engage in an informal system of finance providing capital and credit. Alvarez-Macotela *supra* note 6, at 141 (note 70), 245 and 348.

<sup>73</sup> Alvarez-Macotela, *supra* note 6, at 298.

<sup>74</sup> SAPI is a Limited liability corporation aimed at promoting domestic and foreign investment by providing some protections not established under ordinary company law in Mexico, eg not subject to the supervision of the financial authority; minority shareholders have additional protection such as the right to appoint a director and an examiner, the right to call a meeting having 10 percent of the equity's firm, puts, calls, tag-along, drag-along, etc; SAPIG is a Limited liability corporation, similar to SAPIs but they are expected to become publicly traded in less than three years i.e. a transition vehicle to become a SAB. SAB is a Limited liability corporation publicly traded, i.e. firms that issue shares listed on the MSE.

<sup>75</sup> Other forms of companies than the SAPI, SAPIB and SAB are beyond the scope of this paper. For a 2016 amendment of the company law, introducing a simplified form of public company (SAS), see <http://eleconomista.com.mx/industrias/2016/03/14/publican-ley-general-sociedades-mercantiles>.

ymore!). This new move by the Government of Mexico, and accepted by the private sector, represents a major advance in corporate governance in Mexico.<sup>76</sup>

Though not all of these provisions are perfectly suitable for non-listed companies, the positive effects were apparently regarded as more significant. The blurred division between governance rules for listed and non-listed firms in Mexico has to do with the strategic role that Mexico's government has assigned to the support and promotion of small and medium sized enterprises (SMEs). As these firms employ in excess of 60 percent of the Mexican active population in the formal economy,<sup>77</sup> the Mexican law maker took the view that significant economic growth can only be achieved by approximating the corporate governance standards of SMEs to those of large listed companies.<sup>78</sup>

But, looking at two specific examples, it can be seen that there is some reluctance of Mexican firms to fully adopt practices of good corporate governance. First, the board of directors in the average listed firm has ten members, three of them usually independent and 3 other related to the company. Almost four out of ten board members are also shareholders of the firm, which shows the high percentage of family-owned firms in Mexico. Moreover, some of the top firms in Mexico have boards comprising more than 15 directors, a large proportion of them hold a friendship or close personal connection with members of the controlling family.<sup>79</sup> Second, a study by Deloitte shows that in a series of annual surveys among the top listed and non-listed firms in Mexico one of the topics where there is greater 'opportunity', ie failure in adoption of the Principles, is in the succession plan. The dominant nature of family-firms in Mexico tends to be reflected in a lack of interest to look after such theme. The negative trend identified on that particular topic shows a substantial gap in a culture of prevention and a business vision that helps to separate the family bonds from the working of the businesses.<sup>80</sup> As Bruce Kogut explains about emerging markets: 'governance is exercised through powerful clubs that constitute the social and business networks among owners, directors, and managers. However, the dynamics of simple behaviors can be quite surprising!'<sup>81</sup>

India is a much similar case to Mexico in relation to which the GCGF has recently drawn attention.<sup>82</sup> With some variations and at different degrees, all emerging markets share the challenge of dominant family-businesses and deep-rooted cultural traits on

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<sup>76</sup> S Podolsky, 'Mexico's Corporate Governance Practices in Non-Listed Companies', OECD Paper 2006, available at <http://www.oecd.org/corporate/ca/corporategovernanceprinciples/37329952.pdf>, at p 3. Note: exclamation marks are original from the OECD's paper.

<sup>77</sup> Podolsky, *ibid*, at 5.

<sup>78</sup> KV Kersbergen and F Waarden, "'Governance" as a Bridge Between Disciplines: Cross-disciplinary Inspiration Regarding Shifts in Governance and Problems of Governability, Accountability and Legitimacy' (2004) 43 *European Journal of Political Research* 143 at 147.

<sup>79</sup> OECD, *supra* note 63, at 31.

<sup>80</sup> Deloitte Touche Tohmatsu Limited, '4º Estudio Anual de Mejores Prácticas en Gobierno Corporativo - Contribución de los órganos de gobierno y sus miembros' 2012, available at [www2.deloitte.com/content/dam/Deloitte/mx/Documents/risk/Gobierno-Corporativo/4oEstudio\\_GobiernoCorporativo.pdf](http://www2.deloitte.com/content/dam/Deloitte/mx/Documents/risk/Gobierno-Corporativo/4oEstudio_GobiernoCorporativo.pdf) at p 42.

<sup>81</sup> Global Corporate Governance Forum (GCGF), 'Understanding Cultural and Social Forces is Crucial to Improving Corporate Governance. Interview with Bruce Kogut' (2013), available at [www.ifc.org/wps/wcm/connect/topics\\_ext\\_content/ifc\\_external\\_corporate\\_site/corporate+governance/news/bruce+kogut+interview](http://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/corporate+governance/news/bruce+kogut+interview). See also *infra* note 83.

<sup>82</sup> P Kar, 'Culture and Corporate Governance Principles in India: Reconcilable Clashes?', Private Sector Opinion, Issue 23, 2011, IFC-World Bank and GCGF, available at <https://openknowledge.worldbank.org/handle/10986/11070> at p 6.

which informal institutions relevant to corporate governance are built,<sup>83</sup> a topic further explored in the subsequent section.

## 4. Critical assessment

### 4.1 Substantive fit of the Principles?

It is difficult, or even impossible, to draft laws that are suitable for all countries of the world. The OECD is also aware of this problem, trying to respond to it by contextual initiatives such as the regional roundtables and reports.<sup>84</sup> However, it remains that the Principles are a uniform template which, as the following will explain, does not reflect a model of corporate governance that can simply be applied universally.

More specifically, it is suggested that the Principles are unsuitable for economic environments traditionally dominated by ineffective formal institutions. Market players differ in their expectations about company and securities law depending on their characteristics and motives to take part in the stock market and to engage in other business activities. An important difference exists between those economic agents who acknowledge themselves as members of a group whose dealings in the market are crucially underpinned by personal connections as the source of reciprocal trust (insiders), and those players who do not benefit from such personal ties (outsiders). Because law frequently fails to offer adequate protection to outsiders, informal solutions substitute and compete with legal institutions, sometimes in ways which are convergent with the goals of company and securities law, but often in ways which are not.<sup>85</sup>

The prevalence of family-businesses and related networks is a recurrent theme in scholarly articles and policy-reports on the application of international corporate governance standards in many markets.<sup>86</sup> As such structures are seen as an unfavourable condition to the well working of the market economy, a 'win-win solution' could evolve from reinforced market governance. Yet, family firms may be disinclined to change their strategies simply by market pressures: 'increased governance pressures could make it more costly to indulge in (...) family-centred preferences. Alternatively, better markets for corporate control could allow families to hire professional managers while maintaining the beneficial elements of family ownership.'<sup>87</sup>

In an institutional context where there is no dominant rule of law, associated to lack of credible commitment with regards enforcement,<sup>88</sup> having a family-business is an effective response to the gap in trust in the legal system. It is not a pre-condition opposed

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<sup>83</sup> B Kogut, *The Small Worlds of Corporate Governance*, Vol. 1 (Cambridge, MA: MIT Press 2012); S Claessens and BB Yurtoglu, 'Corporate Governance in Emerging Markets: A Survey' (2013) 15 *Emerging Markets Review* 1; Iu and Batten, supra note 5, at 60.

<sup>84</sup> Kar, supra note 82. See also 3.1 above.

<sup>85</sup> Alvarez-Macotella, supra note 6, at 2.

<sup>86</sup> See generally RK Morck and L Steier, 'Introduction' in *A History of Corporate Governance around the World: Family Business Groups to Professional Managers* (RK Morck ed, Chicago: University of Chicago Press 2005) 1 at p 6: 'Anglo-American shareholder capitalism is exceptional. Other systems predominate (...) the most common system of corporate governance in the world is *family capitalism*'.

<sup>87</sup> M Bertrand and A Schoar, 'The Role of Family in Family Firms' (2006) 20 *The Journal of Economic Perspectives* 73 at 94.

<sup>88</sup> DC North, 'Institutions and Credible Commitment' (1993) 149 *Journal of Institutional and Theoretical Economics* 11 at 19.

neither to a professionalisation in the running of businesses nor to transparency and accountability. Hence, the aforementioned unsuitability does not simply come from family capitalism.

Family or other concentrated corporate ownership structures are common among countries in Central and Eastern Europe, East Asia and Latin America. Yet, the processes and control structures of companies from all those countries are also very different. Furthermore, and contrary to expectations based on the ‘globalisation/convergence’ literature, market-oriented legal and economic reforms in country level governance aimed at promoting investor protection, have not reduced highly concentrated ownership among publicly listed firms in those markets since the adoption of the Principles.<sup>89</sup>

The main rules of the Principles are present in most modern company laws across countries as they apply to publicly traded companies. However, the degree to which they are observed in practice varies much between the leading OECD countries and other countries where informal institutions, corruption, and weak rule of law are dominant features.<sup>90</sup> It follows that designing and implementing the Principles is a remarkable challenge. This explains the growing number of studies and guidelines in order to facilitate the process of integrating the Principles at the micro-level.<sup>91</sup> Yet a main difficulty is to identify functional equivalents (whether formal or informal) in countries with different views and values.<sup>92</sup> It also needs to be ensured that the adoption of the Principles delivers sufficient incentives for the stakeholders and to develop practices to cope with country-specific features of corporate governance.<sup>93</sup>

The Principles are also incompatible with institutional contexts dominated by other informal institutions besides family-ownership, for example, forms of corruption and ways to create opacity in the running of businesses and avoid accountability.<sup>94</sup> The Principles are based on the assumption that those negative elements are usually not present in the OECD member countries. But, for instance, some Mexican entrepreneurs do not find attractive the transparency imposed on public companies for entirely plausible reasons: a significant number of entrepreneurs whose companies could go public belong to strata of Mexican society targeted by organised crime. This argument has explanatory power in particular in the last two decades, when the quality and quantity of information disclosed by public companies has allowed access to sensitive information about some of the wealthiest families in Mexico. In this regard, company and securities laws clash

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<sup>89</sup> RV Aguilera, LR Kabbach-Castro, JH Lee and J You, ‘Corporate Governance in Emerging Markets’, in *Capitalisms and Capitalism in the Twenty-First Century* (G Morgan and R Whitley R eds, Oxford: OUP 2012) 319 at 321, 332 and 339.

<sup>90</sup> O Alvarez-Macotella ‘Mercado Accionario e Instituciones Jurídicas para el Desarrollo’, in *Derecho. Instituciones y Desarrollo* (C Mena, R Robles and JL Velázquez eds, Porrúa 2012) 477 at 510; BS Black, ‘The Legal and Institutional Preconditions for Strong Securities Markets’ (2001) 48 *UCLA Law Review* 781.

<sup>91</sup> See 3.2, above.

<sup>92</sup> For a helpful contribution comparing Islamic and OECD Principles, see Abu-Tapanjeh, *supra* note 4, at 564 and 565.

<sup>93</sup> See Chen et al, *supra* note 5, at 132 and 134, and more generally MI Caron, A Ficici and CL Richter, ‘The Influence of Corruption on Corporate Governance Standards: Shared Characteristics of Rapidly Developing Economies’ (2012) 2 *Emerging Markets Journal* 21.

<sup>94</sup> For the case of Mexico see Alvarez-Macotella, *supra* note 6, at 147-152. For the case of China see H Wang, *Weak State, Strong Networks: The Institutional Dynamics of Foreign Direct Investment in China* (Oxford University Press, Oxford 2001) 169-170.

with a social context in Mexico where kidnapping and violent robberies became common and affect individuals of the upper and middle socioeconomic layers of society.<sup>95</sup>

Furthermore, corporate governance was not a matter of concern for businesses and government leaders in institutional contexts where political rather than business ability used to be more decisive to success, say, in the context of a financial system where bankers chiefly lent to themselves and their family businesses. For example, in Mexico, traditionally, bankers developed the informal institution of lending primarily to themselves and their family members. Credit was restricted to those few entrepreneurs who happened to have family connections with the few people controlling banks.<sup>96</sup>

However, it also needs to be noted that the situation has changed in Mexico (as well as other countries), as some business people want to mirror governance movements taking place in more developed countries. The pressure is also faced by newly privatised companies. The shift to the current interest in good corporate governance comes from a global movement, fostered by the World Bank and the economic literature, seconded by the OECD and related organisations.<sup>97</sup>

In addition, whether the Principles are feasible to adopt or not is perhaps less relevant compared to whether they actually provide sufficient incentives to shift informal agendas and traditional institutions in countries emerging from weak official means of coordination, high ownership concentration and dominant pyramidal control. In those institutional contexts, the role of family firms has been effective to succeed in tunnelling practices from the insider's standpoint as well as in self-protecting from the risk of suffering from it from the outsider's position.<sup>98</sup>

Finally, despite the mixed degree of suitability of the Principles at a global scale, policymakers must respond to the broader shifts in governance. There are growing signs of transition in modes of governance taking place from national to international spheres, but also flowing to sub-national and regional levels. These new forms of networked governance rely on international standardisation bodies complemented by local agencies for implementation and enforcement, as the following will explain.

#### *4.2 The governance model of the Principles: a wicked problem?*

This subsection will analyse and assess the Principles under the category of 'networked governance'. While this is a powerful conceptual device, the following will explain that there is some ambiguity in the way 'networked governance' is understood.

In the literature, there are a number of voices that have related the OECD to the concept of networks. Yet, this has not been done in a uniform way. For example, when the OECD is called a 'catalyst' for the creation of 'transgovernmental regulatory networks',<sup>99</sup> this could mean that the acts of the OECD, such as the Principles, are seen as networks. But some also seem to consider the OECD itself as a network, describing it as

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<sup>95</sup> Alvarez-Macotella, *supra* note 6, at 154.

<sup>96</sup> See S Haber, 'Political Institutions and Financial Development: Evidence from the Political Economy of Bank Regulation in Mexico and the United States', in *Political Institutions and Financial Development* (S Haber, DC North, and B Weingast eds, Palo Alto: Stanford University Press 2008) 10 at 39 and 46.

<sup>97</sup> B Husted and C Serrano 'Corporate Governance in Mexico' (2002) 37 *Journal of Business Ethics* 337.

<sup>98</sup> Chen et al, *supra* note 5, at 132: 'We find that in China, none of the 'good' practices prescribed by the OECD... is effective in attenuating the negative consequences of controlling-shareholder expropriation on corporate performance'.

<sup>99</sup> AM Slaughter, *A New World Order* (Princeton: Princeton University Press 2004) 46.



‘an important institutional network’, being ‘part of the evolving global political super-structure’.<sup>100</sup> Finally, some statements refer to the relations of the OECD to other entities, calling the OECD an important ‘node in the growing networks of transnational governance’ and saying that the evolving networks ‘include other international organizations, appointed experts, and representatives of civil society associations’.<sup>101</sup> Notably, such a network may also define what it means to be a ‘modern state’.<sup>102</sup>

It is suggested that a proper understanding of networks has to relate them to the concept and challenges of governance. One pressing challenge faced by contemporary policymakers is to cope with the rising interdependence between different policy levels and sectors worldwide.<sup>103</sup> The challenge is complex because it implies simultaneously tackling other factors such as a public demand for greater accountability towards the citizens, a general expectation of seeing policies that are technically feasible and acceptable by a new generation of stakeholders which is playing an active role in the policymaking processes, and (closely related to the latter) a growing demand for less vertical interventions.<sup>104</sup> All in all, these factors drive the quest for fresh modes of governance that are effective to manage the potential of networks in a given society.<sup>105</sup>

Not all of the different approaches to governing large human organisations are conducive to a rational exploitation of the resources pooled within those collectivities. The academic debate on networked governance has frequently focused on the concept of policy network in relation to three main modes of governance – vertical, market and networks: ‘vertical’ refers to a top-down structure, depending on a well-organised group with an effective legal system; the ‘market’ model assumes that actors effectively coordinate by self-interest, yet, this depends on necessary incentives for all participants; and by ‘networks’ is meant a series of informal relationships between individuals who see each other as peers, creating an implicit understanding of membership equality and commitment to shared responsibilities built on trust and loyalty.<sup>106</sup> These modes coexist and are interdependent in practice. Hence, the combination of those modalities is crucial since their complementarities and clashes lead to more or less successful outcomes.<sup>107</sup>

The resulting notion of networked governance is built around three components:<sup>108</sup> (i) the interplay between actors from national and international levels as well as from the public and private sectors; (ii) transitions in power relationships where individuals and new organisations are taking over the role of liaising and coordinating with stakeholders and becoming influential in activities previously undertook by well-established hierar-

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<sup>100</sup> Ougaard, *supra* note 37, at 45.

<sup>101</sup> Mahon and McBride, *supra* note 13, at 21; McBride and Mahon, *supra* note 13, at 278.

<sup>102</sup> Porter and Webb, *supra* note 18, at 44.

<sup>103</sup> OECD, *Planning for Sustainable Development: Country Experiences* (Washington DC: OECD Publications 1995) 73.

<sup>104</sup> See A Schout and A Jordan, ‘The European Union’s Governance Ambitions and its Administrative Capacities’ (2008) 15 *Journal of European Public Policy* 957.

<sup>105</sup> A Jordan and A Schout, *The Coordination of the European Union: Exploring the Capacities of Networked Governance* (Oxford: OUP 2007) 56.

<sup>106</sup> Jordan and Schout *ibid* at 15-16. For an overview of the emerging literature on policy networks see also TA Börzel, ‘Organizing Babylon – On the Different Conceptions of Policy Networks’ (1998) 76 *Public Administration* 253.

<sup>107</sup> Börzel *ibid* at 262-263; Jordan and Schout, *supra* note 105, at 17.

<sup>108</sup> This is despite some ambiguity in the scholarly definition which has been acknowledged in dedicated reviews of literature on that topic, eg, Börzel, *supra* note 106, at 254-255.

chical levels, and (iii) growing relevance of co-operative and peer-group decision-making processes and ‘soft-law’.<sup>109</sup> Therefore, the study of networks is offering a way towards politically acceptable means to add value to activities at the domestic level by working closer with countries increasingly interrelated.

On this basis, it can be suggested that the Principles are a good example of networked governance and its possible benefits: they were envisioned in an inclusive process, and the application of the Principles involves a variety of private and public parties, often in a non-hierarchical way. However, against the advantages of networked governance, some of its potential drawbacks may be relevant to the Principles: it does not work well for organisations where hierarchical cultures and, thus, vertical institutions, such as powerful states, are markedly dominant. It is also less effective in settings where stakeholders have dissimilar cultural values and lack of explicit common goals. In addition, as this governance mode coordination is built on trust and loyalty rather than administrative commands (hierarchy) or prices (markets), it matters that trust is primarily a spontaneous phenomenon that takes time to develop.<sup>110</sup>

So what can be done about it? As research by Elinor Ostrom and others has found, cooperation requires trust and needs the support of trust-building institutions such as network management. The interaction between individual parties makes them realise the need for institutions and to identify interdependencies, as well as the need for monitoring mechanisms and independent courts. As a result, they gradually adapt and effective networks emerge built on the basis of a culture of trust.<sup>111</sup>

It could be suggested that such processes can take place in relation to the Principles, given the homogeneity among OECD members, all belonging to the wealthiest countries of the world. However, the membership of Mexico, Chile and Turkey introduces complexity, and deeper complexity is added by the fact that the Principles are aimed at both members and non-members, including countries with considerable lesser democratic and economic development, combined with much greater cultural diversity. To illustrate the point, we can mention the dissimilar levels of overall development, cultural values and governing institutions such as the working of the law from both members (Mexico, Turkey, South Korea) and non-members (eg, India, Indonesia, Brazil and South Africa) compared to the rest of OECD members.

Consequently, the use of the Principles implies going far beyond the task of coordinating a relatively homogenous multinational network. On the contrary, the subject matter shares the features of a so-called ‘*wicked problem*’: it embodies many actors, many administrative levels, many policy phases, and many sectors.<sup>112</sup> Most crucially, the more countries the Principles are intended to cover the greater complexity due to lack of homogeneity. Therefore, the coordination capacities within the multinational setting in

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<sup>109</sup> D Coen and M Thatcher, ‘Network Governance and Multi-level Delegation: European Networks of Regulatory Agencies’ (2008) 28 *Journal of Public Policy* 4 at 50 and 67.

<sup>110</sup> See also 4.1, above.

<sup>111</sup> E Ostrom, *Governing the Commons: The Evolution of Institutions for Collective Action* (Cambridge: CUP 1990); RO Keohane and E Ostrom, ‘Introduction’, in *Local Commons and Global Interdependence: Heterogeneity and Cooperation in Two Domains* (RO Keohane and E Ostrom eds, London: Sage 1995) 1 at 22-23. See also Jordan and Schout, *supra* note 105, at 37; Alvarez-Macotela, *supra* note 6, at 51-52.

<sup>112</sup> See, eg, HWJ Rittel and MM Webber, ‘Dilemmas in a General Theory of Planning’ (1973) 4 *Policy Sciences* 155; L Meuleman, ‘Cultural Diversity and Sustainability Metagovernance’ in *Transgovernance* (L Meuleman ed, Berlin: Springer 2013) 37 at 42 (wicked problems as escaping logics of hierarchies and markets).

question should be seen as interrelated instead of independent. Part of the problem is that, if one level of governance requires the capacities of other levels for the overall system to function effectively, it is uncertain how this affects both the design and use of the coordination mechanisms, as well as its efficacy.

This ‘wickedness’ of the Principles is somehow softened by their flexible nature. When a country decides not to implement them, substitution by private parties will occur as far as the Principles are appropriate for the company in question.<sup>113</sup> By contrast, making the Principles mandatory is problematic if in a particular country such an undifferentiated version of global corporate governance standards does not work well for many of the domestic companies. Thus, in this case it is preferable to let the networked governance of business organisations evolve spontaneously.

## 5. Conclusion

Like its predecessors, the 2015 version of the G20/OECD Principles of Corporate Governance is an example of crisis-driven law making, with the explicit aim to promote financial stability, investment and growth. A possible line of critique may be that failures in corporate governance have not been the main reasons of the financial crisis of 2008,<sup>114</sup> and that the empirical research of whether good corporate governance ‘matters’ for financial development has not produced unambiguous results.<sup>115</sup>

However, regardless of this debate about causal links, it may be laudable that the OECD keeps the Principles up-to-date. The more valid criticism is therefore that the very idea of a global model of corporate governance has its flaws. The foregoing analysis has shown that social, cultural and economic differences play a role at both the country and firm level of corporate governance. As the Principles are based on a common understanding of its member countries, they are likely to be incompatible with institutional contexts dominated by informal institutions, such as family-firm governance, corruption and tricks to veil or obscure the transparency and accountability assumed as the basis of the Principles for the leading OECD countries.<sup>116</sup> Of course, culture is not static. It may change to adapt to the transition in circumstances, as the experience of developed countries shows.<sup>117</sup> But this also requires the corresponding informal institutions, such as an organised civil society where stakeholder engagement plays a fundamental role, something which cannot be assumed in many developing countries.

This critique invites two suggestions on how to transform the nature of the Principles. On the one hand, the suggestion could be to have detailed rules enacted as a binding

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<sup>113</sup> See Figure 1 in 2., above.

<sup>114</sup> For more details see, eg, BR Cheffins, ‘Did Corporate Governance “Fail” During the 2008 Stock Market Meltdown? The Case of the S&P 500’ (2009) 65 *Business Lawyer* 1; S Konzelmann and M Fovargue-Davies M (eds), *Banking Systems in Crisis: The Faces of Liberal Capitalism* (London: Routledge 2012).

<sup>115</sup> For good overviews see G Xu, ‘The Role of Law in Economic Growth: A Literature Review’ (2011) 25 *Journal of Economic Surveys* 833; RV Aguilera and G Jackson, ‘Comparative and International Corporate Governance’ (2010) 4 *The Academy of Management Annals* 485; P Brown, W Beeke and P Verhoeven, ‘Corporate Governance, Accounting and Finance: A Review’ (2011) 51 *Accounting and Finance* 96.

<sup>116</sup> See 4.1, above.

<sup>117</sup> See Morck and Steier, *supra* note 86, at 58 (‘Many countries now considered to have highly trustworthy institutions, including institutions of corporate governance, were profoundly corrupt only a few generations ago.’).

treaty of international law, but that it would then be for companies to decide whether they want to opt into this OECD model of corporate governance, for example, in order to attract international investments. On the other hand, the suggestion could be to transform the Principles into a mere ‘common frame of reference’<sup>118</sup> that has the aim to facilitate the discussion about corporate governance across borders.

This first suggestion seems to have the advantage that it would also address some of the ambiguities of the principles, such as the vagueness of many of its provisions and the unclear target audience.<sup>119</sup> The idea to have the same rules of corporate governance for companies from different countries may also refer to the European Company (SE) as a possible model: here too, companies are not required to use this form of company but can choose it if they want to do so. However, the SE also shows the practical problems with this approach: the common SE rules are very sketchy and few companies have actually made use of this form of company.<sup>120</sup>

The second suggestion is therefore the more realistic one. It is in line with the general trend for more flexible forms of networked governance.<sup>121</sup> Specifically, for the Principles, it can be also be supported by the view that those are a ‘living document’ and that regional roundtables are seen as crucial to assess the usefulness of the Principles in the local context.<sup>122</sup> Thus, to conclude, it is suggested that, contrary to the implementation of the Principles in Mexico,<sup>123</sup> law makers should not transform the Principles into rules of codified company law, but respect their nature as global soft law or even just treat them as a mere ‘common frame of reference’ in the ongoing debate about corporate governance reform.

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<sup>118</sup> This term is inspired by the Common Frame of Reference proposed for a European Contract Law. See [http://ec.europa.eu/consumers/rights/contract\\_law\\_en.htm](http://ec.europa.eu/consumers/rights/contract_law_en.htm).

<sup>119</sup> See 2., above.

<sup>120</sup> See, eg, J Cremers, M Stollt and S Vitols (eds), *A Decade of Experience with the European Company* (Brussels: ETUI 2013).

<sup>121</sup> See 4.2, above.

<sup>122</sup> See 3.1, above.

<sup>123</sup> See 3.2, above.